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UNCLAS SECTION 01 OF 04 PRETORIA 003001

SIPDIS

SENSITIVE

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COMMERCE FOR 4510/ITA/ANESA/OA/JDIEMOND
TREASURY FOR BCUSHMAN

E.O. 12958: N/A
TAGS: ECON EINT ECPS EINV PREL XA SF
SUBJECT: SOUTH AFRICA: HIGH TELECOM PRICES, LITTLE RELIEF IN SIGHT

REF: A. PRETORIA 1441

¶B. PRETORIA 710
¶C. 04 PRETORIA 5556
¶D. 04 PRETORIA 4028

(U) This cable is Sensitive But Unclassified. Not for Internet distribution.

¶1. (U) Summary. President Mbeki condemned South Africa's high fixed telephone line prices in his February 2005 State of the Nation address by stating that they cost ten times more than in developed countries. Mbeki's assertion was mainly directed at Telkom, the de facto monopoly for fixed line telecom and broadband services. The mobile phone market also shares in the blame for high telecom prices despite the fact that three mobile phone operators compete for business. In April 2005, Genesis Analytics completed the latest in a series of studies on high telecom prices in South Africa. Out of the 15 developed and developing comparison countries selected, telecom charges in South Africa were 37% to 399% percent higher than the average costs in 9 out of 10 categories. The South African Government's Department of Communications (DOC) responded by quickly organizing a two-day colloquium on the pricing of telecom services in July. The colloquium concluded that slow steps are being taken in the right direction to reduce high telecom prices, such as the imminent introduction of a Second National Operator (SNO), changing Value-Added Network Service (VANS) provider regulations, the Convergence Bill, and the recent cap of Telkom prices at 3.5 percentage points under inflation. Unfortunately for the consumer, the DOC plans to hold another colloquium in October, which means that little will be done in the immediate future to speed up telecom reforms and introduce effective competition to jump start the industry. End Summary.

Wrong Numbers

¶2. (U) In his February 2005 State of the Nation address, President Mbeki condemned South Africa's high fixed telephone line prices, stating that they cost ten times more than in developed countries. Mbeki's goal was to pressure Telkom, the 38% government-owned de facto monopoly for fixed line telecom services, to lower prices. Since the late 1990s, Telkom has cut costs by slashing jobs and taking on new technology, but has passed on only a fraction of these savings on to the consumer. Consumers have grown increasingly frustrated watching Telkom generate R40.8 billion ($6.5 billion) in revenue and take home R6.3 billion ($1.0 billion) in pre-tax profits in 2004. One of the starkest examples of Telkom's damage is that of the 2.8 million fixed telephone lines rolled out since the late 1990s to serve primarily previously disadvantaged (black) areas, 70% of them have been disconnected for non-payment. Many South Africans simply could not afford the over 300% price increase in peak-rate local calls from 1997 to 2003, and as a result, the number of residential lines per 100 people fell from 6.5 in 1997 to 5.3 in 2003.

¶3. (U) Even though three mobile phone operators compete for business, the mobile market has not fared much better than the fixed line market. The Communications Users Association of South Africa (CUASA) has termed mobile phone charges as "obscene." The telecom regulator, Independent Communications Authority of South Africa (ICASA), noted that Cell C's introduction to the market to compete with Vodacom and MTN did not result in a fall in real prices. (Note: Telkom owns 50% of Vodacom and Vodacom has over a 50% mobile phone market share. All mobile phone operators must make use of Telkom leased lines for calls to landlines, international destinations, and certain national locations. End Note.) On July 18, ICASA released a discussion document on this topic stating its determination to establish whether high mobile charges are justifiable and if regulatory intervention is necessary.

Dialing for Dollars

¶4. (U) A number of studies have highlighted the high telecom prices faced in South Africa when compared to other countries. Genesis Analytics completed the latest assessment of the industry in April 2005. To fend off some of the criticisms of past reports, Genesis compared South Africa to both developed and peer group countries that adhered to "best practices." Developed countries included Canada, Hong Kong, Israel, Norway, Singapore, Sweden, South Korea, and the United States. Peer group countries included Brazil, India, Malaysia, Morocco, Philippines, and Thailand. Below is a summary of how South Africa compared:

Telecom Service	Comparison to Average Cost	Times Greater Than Low Cost
Int'l Leased Lines	399% Higher	31
Business - Local Calls	199% Higher	11
Business - ADSL	148% Higher	9
Retail - ADSL	139% Higher	8
Business - Mobile	107% Higher	23
Domestic Leased Lines	102% Higher	15
Retail - Local Calls	79% Higher	8
ISP Fees	45% Higher	5
Retail - Mobile Calls	37% Higher	11
Business - Int'l Calls	14% Cheaper	3

(Note: ADSL = Asymmetric Digital Subscriber Line allows broadband Internet access over existing copper telephone lines. ISP = Internet Service Provider. Most service comparisons include all 15 countries; however, some comparisons include as few as 11 countries. End Note.)

¶5. (U) The Genesis study painted a grim picture of high telecom prices in the South African market. Charges in South Africa ranked the highest in five of the ten categories. The five categories included Int'l Leased Lines, Business - Local Calls, Business - ADSL, Retail - ADSL, and Domestic Leased Lines. Charges in South Africa were the second highest in Business - Mobile Calls and ranked fourth or fifth highest in the remaining categories. Costs of international calls from South Africa fared the best due to the competition from Voice Over Internet Protocol (VOIP) and call-back options in the market.

¶6. (U) The Genesis study concluded that, while regulatory changes in process are a step in the right direction (Refs A through D), more needs to be done to bring down prices. The study pointed out that no one had yet addressed Telkom's ongoing monopoly of international bandwidth and the non-VOIP voice market. Value-Added Network Service (VANS) providers had gained some regulatory ground, but they had not yet attained a level playing field with Telkom. For example, while VANS could offer VOIP, Telkom still controlled the bandwidth necessary for this service. In addition, Telkom's ISP did not pay the same price as independent ISPs for bandwidth. Overall, Genesis warned of the draining effect high telecom prices would have on the economy and advocated for increased competition in the telecom market and increased ICASA intervention where competition is not feasible.

Can We Talk?

¶7. (U) The South African Government's (SAG) Department of Communications (DOC) responded to public outcry by quickly organizing a two-day colloquium on the pricing of telecom services. On July 14 and 15, the DOC directed a program of speakers and breakout sessions to about 250 participants from the public and private sectors. The speakers included representatives from the DOC, ICASA, and CUASA.

¶8. (U) DOC Deputy Minister Radhakrishna "Roy" Padayachie opened the colloquium calling on everyone to "open (their) minds" in regard to pricing issues in the telecom sector. He emphasized the need to lower the costs for the average citizen and advocated state intervention to merge the first and second economies. Padayachie also stressed the importance of lowering the cost of doing business in order to increase growth and foreign direct investment (FDI) in South Africa. He singled out the call center and outsourcing industries as means to create jobs and curb unemployment. (Note: Industry analysts project that the call center industry could create between 65,000 to 100,000 jobs by 2009. End Note.)

¶9. (U) Padayachie wavered back and forth on whether he thought previous studies had provided appropriate country comparisons for South Africa. The strongest statements he made were that South Africa's prices "could in fact be stated as high" in comparison to other countries and that South Africa compared "very poorly" to Brazil and India. He did state, however, that Telkom's charges, which "could be described as unaffordable," have driven consumers to the mobile market (even though mobile charges are high as well)

and are hampering the roll out of the Internet. In conclusion, Padayachie made his pitch for "collaborative solutions" between the DOC, ICASA, and operators. The DOC's focus in this collaboration will be on policy development and ensuring that an adequate regulatory framework and infrastructure are in place. Padayachie urged ICASA to take a more active role and focus on the Convergence Bill (Ref A) and imminent Second National Operator (SNO) licensing agreement (Ref B). (Note: Padayachie said the SNO licensing agreement would be finalized in a "matter of weeks." End Note.)

¶10. (U) Dr. Tracy Cohen, an ICASA Councilor, took the stage to make a hurried presentation from the regulator's point of view. Cohen began her talk stating that a "much needed dialogue" was needed on telecom pricing. She echoed Padayachie's calls for attracting FDI and improving consumer welfare. She noted ICASA's recent achievements of capping Telkom's prices to 3.5 percentage points less than inflation, upcoming SNO introduction, and VANS regulations. At the same time, Cohen warned that costs will take time to decrease and wondered if more could be done to overcome the regulatory challenges. Cohen announced the July 18 release of a public discussion document on mobile pricing and an upcoming discussion document on ADSL findings. In summary, Cohen expressed ICASA's mutual concern on telecom pricing issues and willingness to play its part in attaining lower, but sustainable prices in the future.

¶11. (U) After government stated its opinions, consumer advocates and operators offered their take on the situation. CUASA representative Ray Webber detailed CUASA's gripes, including the long, unknown wait for the SNO to enter the market, Telkom's lack of per second billing, high mobile phone charges, and the fact that ADSL is out of reach for most users. The five main telecom operators, Telkom, Sentech (wireless Internet provider), Vodacom, MTN, and Cell C, participated in a panel discussion. The operators had little to offer in terms of substance or alleviation from its high prices. Telkom came out on the offensive, highlighting the fact that telecom prices are a small part of inflation, some tariffs are way below international standards, and that it is not making "super economic profits." Telkom also noted that, as of August, its retail ADSL prices will decrease by 30%, its overall prices will be reduced as a result of ICASA's new price cap, and that telecom costs of compliance are high. (Note: In accordance with ICASA's new price cap, Telkom recently presented its revised pricing structure for approval. Telkom plans to reduce overall prices by 3%, however, certain service charges will increase while others decrease. End Note.) Vodacom welcomed public debate on pricing issues; Cell C regurgitated the regulations mobile operators had to comply with, while MTN assured us that its executives were "spending hours on pricing" issues in the boardroom.

Can We Talk Some More?

¶12. (U) At the end of the colloquium's first day, three breakout sessions were held to seek resolution on the issues of policy and regulatory framework, affordable broadband, and affordable universal access. The breakout groups reported their findings back to the group on the second day. The groups commonly expressed the need to for more information sharing with the public, annual benchmarking studies with an agreed comparison group, and making competition effective. Under competition, the groups emphasized the need for unbundled access to local loop telecom lines and facilities and consumer options to readily switch operators.

¶13. (U) The common theme surrounding the colloquium was that steps are being taken in the right direction to reduce high telecom prices, such as the introduction of the SNO, changing VANS regulations, the Convergence Bill, and the recent cap of Telkom prices at 3.5 percentage points under inflation. The pace of the steps, however, needs to be quickened and more can be done. When DOC Deputy Minister Padayachie closed the colloquium, he crushed this promising theme in describing the way forward. He announced that there would be another colloquium on this issue held on October 14 - 16. The October meeting would be held to discuss the paper from the first colloquium, prioritize issues from this paper, and gather further input from peer countries. Padayachie went on to take nominations for a telecom pricing working group to address these issues and mentioned plans of completing more benchmark studies by the end of the year. Essentially, the DOC plans to hold another meeting to discuss the first meeting and do additional analysis on this topic. This plan fulfills the breakout groups' desire to increase information sharing and conduct additional studies. This plan, however, does nothing to expedite current reforms in place or provide a roadmap to effective telecom competition in South Africa.

Comment

¶14. (SBU) This colloquium had great promise, but failed to bring about potential long-term resolutions to high telecom prices. The DOC seems intent on continuing to identify and study the problem ad nauseam instead of implementing efficient and effective solutions. Conducting another study is going to result in telling the DOC, ICASA, and the operators what they already know -- effective competition needs to be introduced so that telecom prices can be reduced. Without these measures, universal affordable access will never be attained and foreign business will continue to invest elsewhere. The real work lies in identifying the best way to implement effective competition and let private sector led growth lead the charge.
HARTLEY